ANALYSIS OF ORIGINAL BILL

Franchise Tax Board

Author:	Bill Campbell	Analyst:	Gloria McConnell	Bill Number:	AB 2414
Related Bills:	See Legislative History	Telephone:	845-4336	Introduced Date:	02/21/02
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Statute of Limitation on Collection Actions

SUMMARY

This bill would preclude the Franchise Tax Board (FTB) from collecting individual personal income tax (PIT) liabilities that are more than 10 years old.

PURPOSE OF THE BILL

According to the author's office, the purpose of this bill is to give California's taxpayers the same tax relief under state law that is given to them under federal law.

EFFECTIVE/OPERATIVE DATE

This bill would be effective on January 1, 2003. However, it would be operative with respect to assessments of tax that are final on or after January 1, 1994.

POSITION

Pending.

ANALYSIS

FEDERAL/STATE LAW

Under both federal and state income tax laws, in general, if taxpayers have delinquent tax amounts, a lien arises (statutory lien) for that amount upon all real and personal property belonging to that taxpayer. For federal purposes, this statutory tax lien exists as long as the delinquency exists or until it is unenforceable by reason of lapse of time. For state purposes, the statutory tax lien exists as long as the delinquency exists. A notice of federal or state tax lien may be recorded or filed as provided by law.

Under federal law, the Internal Revenue Service is precluded from taking any collection action 10 years after the assessment of tax. The 10-year limitation on collection is extended or suspended under a number of circumstances, such as bankruptcy actions, installment agreements, offers in compromise, wrongful levies, or pending court actions. The federal 10-year limitation applies to all taxpayers: individuals, as well as all other taxpayers.

Board Position:			Department Director	Date
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Under current state law, there is no statute of limitation (SOL) on the collection of an income tax delinquency.

CURRENT PRACTICE

As a result of FTB's current collection practices, including its automated collection system, virtually all tax delinquencies remain subject to collection until full payment is made. Attachment A provides details relating to FTB's current collection practices.

THIS BILL

This bill would enact a 10-year SOL on collection actions against individuals comparable to that provided under federal law. However, levies and notices of tax liens issued during the 10-year collection period would expressly continue in effect until they expire. Once the 10-year collection SOL expires, levies or notices of state tax liens could not be issued or renewed. Additionally, in cases that are in probate or where taxpayers file bankruptcy or owe child support debts, the 10-year collection SOL would be extended. This extension would be comparable to that allowed under federal law.

Further, the annual written notice of tax delinquency required to be sent to taxpayers under the Taxpayers' Bill of Rights, would only be sent during the 10 years that a delinquency is subject to collection, which is also comparable to federal law.

IMPLEMENTATION CONSIDERATIONS

Because the effects of this bill won't begin to occur until January 1, 2004, staff would have one year to program and test the changes to FTB's systems. Implementation of this bill should not be problematic. However, the following concerns have been identified with respect to the funding of the programming and testing costs:

- The programming and testing activities would have to begin during the latter half of fiscal year 2002-03 (January 1, 2003 through June 30, 2003), which would require an appropriation in the bill to ensure funding for these activities.

- With the short, six-month time-frame in fiscal year 2002-03, it is difficult to know exactly what specific activities will be performed, and the associated costs that will be expended in that six-month period. Therefore, staff suggests that the appropriation language specify that any appropriated amounts not encumbered by June 30, 2003, could be expended in the subsequent year.

LEGISLATIVE HISTORY

SB 2171 (Senate Revenue and Taxation Committee; 2000) had the same 10-year collection SOL provisions as this bill, but the provisions were amended out of the bill prior to it being heard in its first policy committee.

OTHER STATES' INFORMATION

Five of the larger states with personal income tax laws similar to California's were reviewed. The collection SOL provisions for these states, in general, are as follows:

State:	*Illinois*	*Massachusetts*	*Michigan*	*Minnesota*	*New York*
Period:	20 years	No SOL	No SOL	5 years	6 years

FISCAL IMPACT

Departmental Costs

As addressed under "Implementation Considerations," an implementation plan will be subsequently developed and the resulting departmental costs determined. However, for SB 2171, departmental costs were estimated for such a 10-year collection SOL provision. This estimate may still be relevant for discussion purposes only, given that the department's current practices and affected automated systems have not significantly changed. Under that estimate, the departmental costs would range from approximately $200,000 to $250,000, for each of the two fiscal years following enactment of the bill.

ECONOMIC IMPACT

Collection Estimate

The amount of tax liability that otherwise would be collected beyond the 10-year collection SOL proposed by this bill would determine the revenue impact of this bill. Staff reviewed the collection estimate that was prepared for the 10-year collection SOL provision that was in SB 2171. The collection data for that estimate appears to be relevant for this bill given that current practices of the department has not significantly changed. Under this assumption, it is projected that this bill would result in a PIT revenue loss of approximately $10 million annually. Because this bill applies with respect to assessments of tax that are final on or after January 1, 1994, the revenue losses would begin after January 1, 2004.

Collection Discussion

This collection estimate was developed from various methodologies using data extracted from FTB's accounts receivable files and other relevant information sources. The methodologies took into consideration, among other things, the amount of revenue that was collected by FTB on accounts that were more than 10 years old.

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Attachment A

FTB currently uses an automated billing/collection system to collect the majority of its delinquent accounts. Taxpayers with tax delinquencies receive one or more notices that range from notices of tax due, to notices that provide that continued failure to pay will result in additional collection actions, to notices of state tax liens. FTB's notices of state tax liens are routinely issued on PIT delinquencies when the amount is sufficient to warrant such action. Such notices are recorded in the county where the taxpayer's real property, if any, is located. On a case-by-case basis, notices of state tax liens may be renewed within 10 years of the date the notice of state tax lien is recorded/filed. If taxpayers continue to fail to pay their tax delinquency, FTB may issue orders for employers or banks to withhold delinquent taxes form wages or accounts, respectively. In general, an order for employers to withhold wages creates a lien on the taxpayer's wages for one year, whereas for bank accounts the order is valid only at the time of receipt. Continuous orders to withhold are issued by FTB when the asset or value of that asset is ongoing. A continuous order to withhold does not expire until the earlier of either the date the delinquency is satisfied or the asset has no further value.

If after several years, FTB cannot locate assets belonging to the debtor and determines that the chances of collecting a delinquency would be remote, the account may be discharged from collection accountability pursuant to the Government Code. Once a delinquency is discharged from collection accountability, FTB generally discontinues any manual efforts to collect the delinquency. However, in the event an employer, a bank account, or any other readily accessible asset is identified, FTB uses its automated system to issue levies on those assets. In addition, if an overpayment of tax from another tax year is subject to refund, the overpayment is applied against the discharged delinquency before any remaining overpayment is refunded.